

IN THE HIGH COURT OF JUDICATURE AT MADRAS

DATED : 14.06.2007

Coram :

THE HONOURABLE MR.JUSTICE P.D.DINAKARAN

AND

THE HONOURABLE MR.JUSTICE P.P.S.JANARTHANA RAJA

Tax Case (Appeal) Nos.609 and 610 of 2007

Commissioner of Income-tax-VI,
Chennai.

..Appellant in
both the T.C.(A)s.

Vs.

VGR Foundations,
Flat No.6,
31, II Main Road,
Kasturba Nagar,
Chennai-20.

..Respondent in
both the T.C.(A)s.

Appeals under Section 260A of the Income-tax Act, 1961 against the order of the Income-tax Appellate Tribunal, 'B' Bench, Chennai in I.T.A. Nos.5/Mds/2003 and 906/Mds/2003 dated 15.07.2004, for the assessment year 1997-98 and 1998-99 respectively, against the order of the Commissioner of Income Tax Appeal VII chennai in ITA.No.71/02-03 dated.27.11.2002, and the order of the Commissioner of Income Tax Appeal-VIII, Chennai in ITA.No.68/02-03 dated 21.3.2003, against the order in PAN/GI.No.752428-V of Income Tax officer, ward V(4) Chennai-34, Assessment order 1997-98 dated 14.3.02 the order in PAN/GI.No.752428-V OF Income Tax Officer, WardV (4, Chennai-34 Assesment order of 1998-99 dated 14.3.02.

For Appellant : Mr.T.Ravi Kumar,
Standing Counsel for
Income-tax Department

JUDGMENT

(Judgment of the Court was delivered by
P.P.S.Janarthana Raja, J.)

These appeals are filed by the Revenue against the order of the Income-tax Appellate Tribunal, 'B' Bench, Chennai in I.T.A. Nos.5/Mds/2003 and 906/Mds/2003 dated 15.07.2004, raising the following common substantial question of law:-

Whether on the facts and in the circumstances of the case, the Income Tax Appellate Tribunal was right in holding that interest on moneys borrowed for the period prior to the commencement of business can be allowed as deduction from the interest u/s 57 of the Act while computing "Income from Other Sources" in respect of the interest received?

2. The facts leading to the above substantial question of law are as under:

The assessee is a Partnership Firm, engaged in the Real Estate business. The relevant assessment years 1997-98 and 1998-99 and the corresponding accounting years ended on 31.03.1997 and 31.03.1998, respectively. A survey under Section 133A of the Income-tax Act ("Act" in short) was conducted on 27.1.2000. Notices under Section 148 were issued on 09.03.2000. The assessee-firm filed "nil" Returns of Income and also filed letters stating that the Returns filed vide Acknowledgement No.8869 dated 14.02.2000 for the assessment year 1997-98 and Acknowledgement No.8871 dated 14.02.2000 for the assessment year 1998-99, have to be treated as Returns in response to the notices issued under Section 148 of the Act. Further, notices under Section 143(2) were issued on 20.11.2001. The Assessing Officer noticed that the statements filed along with the Returns of income reveal that the assessee had incurred expenses prior to commencement of business and the assessee had also earned interest income from out of the fixed deposits with bank and the said income had been set off against the expenses. The Assessing Officer was of the view that the interest received on short term deposits in bank during pre-production stage is assessable as income from other sources. Hence the same was considered as income from other sources, determining the total income at Rs.1,59,350/- and Rs.1,16,400/- for the assessment years 1997-98 and 1998-99, respectively. Aggrieved by the orders, the assessee filed appeals to the Commissioner of Income-tax (Appeals). The C.I.T.(A) dismissed the appeals and confirmed the orders of the Assessing Officer. Aggrieved, the assessee filed appeals to the Income-tax Appellate Tribunal ("Tribunal" in short). The Tribunal allowed the assessee's appeals and set aside the orders of the C.I.T.(A). Hence the present tax cases by the Revenue.

3. Learned Standing Counsel appearing for the Revenue submitted that the assessee had set off interest earned, prior to commencement of the business operation, against the expenses. The assessee is wrong in setting off the interest prior to the commencement of the business operation against expenses. The interest income earned prior to commencement of the business has to be assessed under the head "income from other sources". Hence, the Assessing Officer is right in assessing the interest income under the head "income from other sources".

4. Heard the counsel. The Tribunal allowed the appeals by following its own earlier order and accepted the contention of the assessee. The Tribunal, in its order, held as follows:-

"5. Before me the learned counsel for the assessee also relied on the decision of the Supreme Court in the case of CIT v.

Karnataka Power Corporation (247 ITR 268) (SC), wherein it was held that interest receipts / hire charges received during pre-production is on capital account. The learned counsel for the assessee also relied on various decisions in support of his case. At the time of hearing he had also filed a copy of the order of this Tribunal in I.T.A. No.1369/Mds/02 dated 11-11-2002 wherein on identical issue the Tribunal considering the various Supreme Court decisions observed and held as under:-

"4. The Supreme Court in Tuticorin Alkali Chemicals and Fertilizers Ltd. (supra) was considering investment of borrowed funds prior to commencement of business and held that the interest earned was taxable. In Bokaro Steel Ltd. (supra), it was a case of a Govt. company which during the period of construction of the plant had advanced monies to contractors on which it was earning interest, received rent from quarters let out to employees, received hire charges on plant let out to contractors and received royalty on stones removed from the assessee's lands. The Supreme Court considered all these activities to be intricately connected with the construction activity and accordingly held that interest received, rent received, hire charges and royalty etc. would be reduced from the cost of the assets and it would not be treated as income. Similar view was expressed by the Supreme Court in the case Karnal Cooperative Sugar Mills Ltd. (supra). Identical view was also taken by the Supreme Court in the case of Bongaigaon Refinery and Petrochemicals Ltd. and Karnataka Power Corporation (supra).

5. In our opinion, in view of the above clear cut ruling by the Supreme Court it is necessary to give a finding of fact in regard to monies that were kept in deposit from out of the share application monies. In the light of the Supreme Court decision in Tuticorin Alkali Chemicals and Fertilizers Ltd. (supra), it is only in the event of interest earned from out of deposits made from borrowed funds that it would be in the nature of income. Share application monies do not fall into the category of borrowed funds and do not involve payment of interest. In effect share application monies etc. are gathered for being used in setting up of an industry, unit, purchase of assets, and so on. Till such time the money is required for deferment of various items, obviously the money has to be kept in deposit with a bank. Keeping the money in current account would not yield any interest income. It can therefore be seen that it is during the course of construction that the monies are kept in deposits with the bank. In these circumstances in the light of the Supreme Court decisions in the cases of Bokaro Steel Ltd. (supra), Karnal Co-operative Sugar Mills Ltd. (supra) and Karnataka Power Corporation (supra),

the claim of the assessee is reasonable and deserves to be accepted. We accordingly uphold the claim of the assessee and delete the addition of interest made to the income. The legal plea was not insisted upon."

From a reading of the above, it is seen that the Tribunal has followed the principles enunciated in the Supreme Court judgments in the case of C.I.T. Vs. Bokaro Steel Ltd. (236 ITR 315) and in the case of C.I.T. Vs. Karnataka Power Corporation (247 ITR 268) and came to the correct conclusion. The Revenue is unable to give any further materials or evidence and also not able to furnish information as to whether they have filed any appeal against their earlier order or not.

5. Under the circumstances, we do not find any error or legal infirmity in the order of the Tribunal so as to warrant interference. Hence, no substantial question of law arises for consideration of this Court and accordingly the tax cases are dismissed. Consequently, M.P.No.1 of 2007 in T.C.(A) No.610 of 2007 is closed. No costs.

km

Sd/-
Asst.Registrar

/true copy/

Sub Asst.Registrar

To

1. The Assistant Registrar,
Income-tax Appellate Tribunal, 'B' Bench,
Chennai.
2. The Commissioner of Income-tax (Appeals) VIII,
Chennai.
3. The Commissioner of Income-tax (Appeals) VII,
Chennai-600 034.
4. The Income-tax Officer,
Ward V(4), Chennai-34.
5. The Commissioner of Income tax -VI , Chennai.

+1 cc to Mr.N.Muralikumaran,Advocate Sr.No.34893.

SA(CO)
dcp/2.7.07

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